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IN THE

Supreme Court of the United States.

OCTOBER TERM, A. D. 1933.

No. 400.

CITY OF MARION, ILLINOIS, a Municipal Corporation; CONTINENTAL ILLINOIS BANK & TRUST COMPANY, a Corporation; THE FIDELITY & CASUALTY COMPANY OF NEW YORK et al.,

Petitioners,

versus

BEN SNEEDEN, as Receiver of the City National Bank of Herrin, Illinois,

Respondent.

Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

BRIEF OF RESPONDENT.

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Respondent.

Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

BRIEF OF RESPONDENT.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Ben Sneeden, as Receiver of the City National Bank of Herrin, Illinois, the above-mentioned respondent, respectfully presents the following as his brief in the above-entitled cause.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals is reported in 64 Fed. (2d) 721, and appears on pages 101-118 of the record. The dissenting opinion of Judge Alschuler is on pages 118-126 of the record. The opinion of the District Court is reported in 58 Fed. (2d) 341, and is on pages 55-62 of the record.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered April 25, 1933 (R. 127). Petition for rehearing was denied June 1, 1933 (R. 128). Certiorari was granted October 16, 1933, under Section 240a of the Judicial Code as amended by Section 1 of the Act of February 13, 1925 (C. 229, 43 Stat. 936, 938).

STATEMENT OF CASE.

We wish to add the following to petitioners' statement of the case:

This case is tried upon an agreed stipulation of facts (R. 2 and 31). The deposits in question were made between August 25, 1931, and October 21, 1931. The bank failed October 21, 1931, instead of October 31, 1931, as stated on page 5 of petitioners' brief, and respondent Sneeden was appointed Receiver.

The City National Bank of Herrin did not at any time

execute to the City of Marion, Illinois, a bond in any form whatsoever securing the city's deposits. Petitioners state on page 4 of their brief that when these transactions were consummated on August 28, 1931, there was no question concerning the sound financial condition of the bank and that the pledge of the assets of the Herrin bank was authorized by the board of directors and was ratified by it after the pledge was made. No reference was made in the stipulation of facts concerning the financial condition of the Herrin bank. The claimed ratification by the board of directors was made by the cashier talking over the matter individually with various directors at board meetings and the directors acquiescing therein, although no formal action was taken by the board.

Petitioners state the questions involved are (Petitioners' Brief, p. 5):

> 1. Does a national bank have general power to pledge assets as security for deposits of public moneys of states or political subdivisions thereof?
>
> 2. Does the amendment of June 25, 1930, to Section 5153, Revised Statutes, limit the power of a national bank to pledge assets as security for deposits of public moneys of a state or political subdivision thereof, to that possessed by state banks in the state in which the national bank is located?
>
> 3. Do state banks of Illinois have general power to pledge assets as security for deposits of public moneys of the state or any political subdivision thereof?

There should be added to these questions the following:

4. Has a bank, either national or state, located in the State of Illinois, power to pledge its assets to secure the deposits of public moneys of a city organized under the Illinois Commission Form of Government Act?

5. Did the City National Bank of Herrin have the right to pledge its assets as security for the deposit of public moneys of the City of Marion?

Respondent insists that the first, third, fourth and fifth questions should be answered in the negative and that the second question should be answered in the affirmative, and we further insist that under the facts proved in this case the respondent is entitled to the equitable relief which he prayed in his bill.

SUMMARY OF ARGUMENT.

The United States Government has no sovereign right to priority of payment of debts due it, and if the Government desires to exercise such right Congress must pass the necessary legislation.

In Illinois the common law is in force and the State is entitled to priority of payment of state deposits in insolvent state banks; this priority, however, does not extend to the political subdivisions of the state.

National banks are governed by national and not by state laws and a state cannot by enacting a state statute

secure a priority for the deposits of the state, or a political subdivision thereof, in an insolvent national bank.

The power to receive deposits conferred upon a national bank by the National Bank Act did not give the national bank power to pledge its assets as security for such deposits.

Power was granted a national bank to secure United States deposits by Section 45 of the National Bank Act, and by subsequent acts of Congress.

The amendment of 1930 was passed because various courts and state officials were taking the position that the action of the Comptroller of the Currency in permitting national banks to secure deposits of states and political subdivisions thereof was unlawful and not authorized by Congress.

Neither by the Constitution nor by any statute has the State of Illinois granted to an Illinois bank the right to secure the deposit of a city by pledging the assets of the bank.

All powers of a bank must be those that are conferred in express terms by the statute or by necessary implication. Neither national nor state banks have any implied power to pledge their assets to secure deposits and it is against sound public policy that they should have such right. Instead of such right being necessary and helpful to their business it leads to their insolvency and ruin.

There is a wide difference between the relation the bank bears to its depositors and that the bank bears to those

from whom it has borrowed money. Outside of each bearing the relation of debtor and creditor, their interests are exactly the opposite.

In the case of Ward v. Johnson, 95 Ill. 215, the so-called deposit was simply a loan of money to the bank.

The Illinois Commission Form of Government Act and the amendment of June 25, 1930, of the National Bank Act, constituted the sole authority and prescribed the only method by which the City National Bank of Herrin, Illinois, could lawfully secure the deposit in question of the City of Marion, Illinois.

The pledge was ultra vires, unlawful and void. The City was a party to the unlawful transaction and must now share with the other creditors the losses of the bank and be content with its dividends.

The burden of proof is upon petitioners to show that the bank had the power to make the pledge and not upon the respondent to show that the bank did not have the power. Both the law and the equities of the case are with respondent, who represents the creditors of the bank, and the decree of the United States Circuit Court of Appeals should be affirmed.

ARGUMENT.

POINT I.

United States Government Has no Sovereign Right to Priority of Payment of Debts Due It, But Such Right Depends Upon Acts of Congress.

It has been the consistent holding of the federal courts that the United States Government has no inherent or sovereign right to the priority of payment of debts due the Government. Such right, of course, the Federal Government may exercise at any time it desires to enact a law to that effect, but in order to secure such priority the Federal Government must, by an act of Congress, take unto itself such right (United States v. Bank of North Carolina, 6 Pet. 29; United States v. State of Oklahoma, 261 U. S. 253; Mellon v. Michigan Trust Company, 271 U. S. 236).

POINT II.

The State of Illinois Has a Right of Priority of Payment of Debts Due It by Virtue of Its Sovereign Powers.

In the State of Illinois the common law is in force, and the Supreme Court of Illinois has held that as to funds of the State of Illinois, the state has prior claim upon the assets of an insolvent state bank, but that this claim applies only to state funds and does not extend to the funds of the various political subdivisions of the state, such as

counties, townships, cities, school districts, etc. (People v. Farmers State Bank, 335 Ill. 617; People v. Ohle, Receiver, 345 Ill. 405).

It therefore follows that in Illinois a municipality has no inherent or sovereign right to priority of the payment of its funds in an insolvent state bank, and that any right of the bank to secure such funds must come from the statutory powers, express or implied, of such bank.

POINT III.

National Banks Are Governed by National and Not by State Laws.

National banks are not private corporations whose principal object is individual trade and profit, but are public corporations created for public and national purposes. They are "instruments designed to be used to aid the Government in the administration of an important branch of the public service" (McCullough v. Maryland, 4 Wheat. [U. S.] 316; Osburn v. Bank of United States, 9 Wheat. 738; Farmers and M. National Bank v. Dearing, 91 U. S. 29).

National banks are governed by national and not by state laws and the power of a national bank to secure a city's deposit by pledging the assets of the bank must be derived from the statutory power, either express or implied, granted to the national bank by Congress. A state has no right by statute to control the operation, manage-

ment or liquidation of a national bank in any respect, nor can a state, by its own statute, secure a priority for debts due the state or any political subdivision thereof from an insolvent national bank (Cook County National Bank v. United States, 107 U. S. 445, 2 Sup. Ct. 561; Davis v. Elmira Savings Bank, 161 U. S. 57, 16 Sup. Ct. 502; Easton v. State of Iowa, 188 U. S. 220, 23 Sup. Ct. 288).

POINT IV.

National Banks Have No Power to Pledge Assets to Secure the Deposit of Municipal Funds in the Absence of the 1930 Amendment.

The general powers of a national bank are found in Section 8 of Chapter 106 of the Act of 1864 (13 Stat. 99, 101, Sec. 5136, R. S.), which provides the association shall have power "* * * Third. To make contracts, * * * Seventh. To exercise by its board of directors, or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; * * *."

It being the law that the United States Government does not have any inherent or sovereign right of priority in the payment of debts due the United States, Congress evidently considered it necessary to provide that United States deposits should be secured by pledging the assets of national banks, because, in the Act of Congress of 1864

above mentioned, in section 45, chapter 106 (13 Stat. L. 113, R. S. 5153) it is provided as follows:

> "All national banking associations, designated for that purpose by the Secretary of the Treasury, shall be depositaries of public money, under such regulations as may be prescribed by the Secretary; and they may also be employed as financial agents of the Government; and they shall perform all such reasonable duties as depositaries of public money and financial agents of the Government as may be required of them. The Secretary of the Treasury shall require the associations thus designated to give satisfactory security, by the deposit of United States bonds and otherwise, for the safe-keeping and prompt payment of the public money deposited with them, and for the faithful performance of their duties as financial agents of the Government * * *."

Congress has also from time to time passed various other acts relating to the giving of security by national banks and by state banks for the deposits of funds in the hands of United States officers. These statutes are set out in petitioners' brief.

It is evident that in Section 8 of the National Bank Act of 1864 Congress did not grant to a national bank any express power to pledge its assets to secure deposits, either public or private, and that the power of a national bank to pledge its assets to secure deposits of United States funds is derived from Section 45 of the Act of 1864 and the subsequent acts of Congress. It is therefore ap-

parent that the other acts of Congress instructing officers of the Government to require a pledge of assets to secure the deposits of Government funds, in so far as national banks are concerned, is a utilization of the power granted national banks under section 45 and not of any supposed power granted under section 8.

Section 45 of the Act of 1864 (R. S. 5153), prior to the 1930 amendment, did not give a national bank any express authority to pledge its assets to secure public deposits, excepting those of the United States Government.

Prior to the 1930 amendment, it is evident the public money referred to in section 45 was public money of the United States Government, and that section 45 authorized the pledging of assets only to secure funds of the United States.

Apparently, the Comptroller of the Currency had taken the position that national banks, prior to the 1930 Amendment, had the right to give security for the safekeeping and prompt payment of public moneys of a state or any political subdivision thereof. It is apparent from the proceedings had in the Senate and the House concerning the 1930 Amendment, as shown in note 1 on page 23 of petitioners' brief, that several courts and various state officers had taken the position that such pledges by national banks were unauthorized by law and were invalid. Therefore, Congress, in 1930, sought to give national banks the express statutory power to secure deposits of the state and political subdivisions thereof. In order to do this,

section 45, above mentioned, was amended (on June 25, 1930) by adding thereto the following provision:

> "Any association may, upon the deposit with it of public money of a state or any political subdivision thereof, give security for the safekeeping and prompt payment of the money so deposited, of the same kind as is authorized by the law of the state in which such association is located in the case of other banking institutions in the state."

That Congress sought to give national banks additional powers to secure public deposits is borne out by the fact that the above was enacted as an amendment of section 45, which gave the national banks the power to secure United States Government funds.

Petitioners, in point two of their brief, and Judge Alschuler, in his dissenting opinion, set forth on page 25 of petitioners' brief, contend that the 1930 Amendment gave national banks additional power to pledge over and above the broad, general powers which it is claimed they already had. We find it difficult to follow the reasoning of petitioners and Judge Alschuler on this point. If national banks already had the broad, general power to secure the deposit of public funds by pledging their assets, what use or necessity was there in Congress passing the 1930 amendment? If national banks already had such broad and unrestricted power to pledge their assets to secure public deposits, Congress by passing the 1930 amendment not

only failed to enlarge their powers, but, in fact, restricted such powers, in that the 1930 amendment restricts or narrows this right to the extent that a national bank is authorized to secure deposits of public funds of states or subdivisions thereof only in the same manner as is authorized by the law of the state relating to other banking institutions where the national bank is located.

If the contention of petitioners is correct, it will be noted that Congress, instead of clarifying the law upon the subject, made the situation more confusing. We submit that if Congress had intended to clarify the law to permit pledges of assets to secure the deposits of states and political subdivisions thereof, leaving the broad, general powers which it is claimed national banks then had still in existence, it would have enacted the 1930 amendment without the following clause:

> "of the same kind as is authorized by the state in which such association is located in the case of other banking institutions in the state."

It will be noted that the doubts referred to in the correspondence set forth in note 1 on page 23 of petitioners' brief had not arisen by reason of any law enacted by any state attempting to prohibit national banks from pledging their assets, but the doubts mentioned were that Congress had given national banks such power.

Judge Alschuler, in his dissenting opinion (page 25 of petitioners' brief), states that the amendment was enacted

to remove any prior inhibitions upon national banks from doing some or any of the things in that regard which might in some particular state be done by the state banks thereof. If national banks prior to the 1930 amendment already had broad, general and unrestricted powers to secure public deposits of the state and its political subdivisions, what inhibitions were there or could there be upon the power of national banks? Neither petitioners nor Judge Alschuler in his dissenting opinion pointed out any such inhibitions. If there were any inhibitions on the claimed broad, general power, such must necessarily have been created by acts of Congress and could be definitely cited.

Since the amendment of 1930 national banks have power to secure deposits of a city only in case a state bank is authorized by the law of the state to secure such deposits. Assuming, for the sake of argument, that the City National Bank of Herrin, prior to the 1930 amendment, had the broad and general power to secure the deposit of the funds of the City of Marion, Illinois, by pledging its securities, then we submit that, by the amendment of 1930, Congress has provided in substance that the City National Bank of Herrin did not thereafter have such right unless a state bank in the State of Illinois was authorized by the law of the State of Illinois so to secure such deposits.

Where a particular statute grants a power and limits the mode of exercising it, it negatives the exercise thereof by any other method (Botany Worsted Mills v. United

States, 278 U. S. 282, 49 Sup. Ct. Rep. 129). We quote from the case of Stephens v. C. B. & Q. R. R. Co., 303 Ill. 49, on page 54, as follows:

> "Where, therefore, there is in the same statute a particular enactment and also a general one, which in its most comprehensive sense would include what is embraced in the former, the particular enactment must be operative and the general enactment must be taken to affect only such cases within its general language as are not within the provisions of the particular enactment. It follows that where an act in one set of provisions gives specific and precise directions to do a particular thing, and in another set prohibits, in general terms, the doing of that which in the broad sense of the words used in the latter would cover the particular act authorized by the former, the more general provisions cannot be deemed to include the matters embraced in the more specific ones" (citing Endlich on "Interpretation of Statutes," Sec. 399).

If we assume that Section 8 of the Act of 1864 granted the City National Bank of Herrin the general and broad power to secure the deposits of the funds of the City of Marion, Illinois, by pledging its assets, then the amendment of 1930 restricted this right and gave the City National Bank of Herrin such right only in case a state bank in Illinois had the same right. The contention of petitioners is, in substance, that a broad, general power existed; that doubt of such power was entertained, and that Congress, by the 1930 amendment, intended to remove

doubt as to the existence of part of that broad power and leave everyone still in doubt as to existence of the remainder. Surely, no such intention can be attributed to that legislative body.

Petitioners, under Point One of their brief, entitled, "National banks have always had power to pledge their assets as security for deposits of public funds," cite the case of Smith v. Lansing, 22 N. Y. 520. That case upheld the validity of pledges to secure both public and private deposits. The Smith case did not involve a national bank and was decided prior to the enactment of the National Bank Act in 1864. It therefore can be no authority for the contention of petitioners that national banks have always had the power to pledge assets as security for deposits of public funds. It cannot be contended that Congress in enacting the National Bank Act took into consideration the decision of one of the states in reference to state banks. The Smith v. Lansing case, in so far as it applied to private deposits, has not been followed by the courts of New York. The case of State Bank of Commerce v. Stone, 261 N. Y. 175, 184 N. E. 750 (cited by petitioners on page 46 of their brief), decided February 28, 1933, expressly held that a New York state bank had no authority to pledge its assets to secure private deposits, and the Court further said with reference to public deposits as follows:

> "Whatever doubt there may have been regarding the power of banks to secure the deposits of **public**

moneys has been removed by statute (State Finance Law; Cons. Laws, c. 56, #8; L. 1909, ch. 10, #44; County Law, #145; L. 1931, ch. 419; L. 1932, ch. 97; and Greater New York Charter, #196). An act of the Legislature was evidently thought necessary, even as to public moneys, to enable banks to pledge certain securities for undertakings or deposits. Such were the last three enactments above mentioned (**Matter of Carnegie Trust Co.**, 206 N. Y. 390)."

The case of United States v. Robertson, 5 Pet. (U. S.) 641, decided in 1831, is ably discussed by Judge Sparks in the opinion heretofore rendered in the case at bar, who points out that neither counsel raised the point as to the power of a banking association to pledge its assets nor did the Court notice it, and on this point we quote from the dissenting opinion of Justice Baldwin referred to by Judge Sparks, as follows:

"I cannot consider this (the pledge) as anything short of a palpable perversion of the corporate powers of the directors, by depriving innocent individuals of every possible right. • • • The power to manage, control and dispose of corporate property is a special authority given by the charter. None can be exercised which is not explicitly granted; and it can only be exercised on the precise subjects over which it is given, and within the limits definitively assigned. • • • The injured creditors are not bound to show a negative of the power by any restrictions or prohibitions. It is an universal principle that he who claims under a special authority must show its existence and lawful exercise: to throw the burthen of proof on the

party whose rights will be destroyed by its abuse, would be the utter reversal of every rule which governs the execution of powers."

Justice Baldwin also stated, as to abuses of corporate powers by the agents of a corporation:

"* * * it follows, necessarily, that in so doing their acts are void as to the bank, and cannot operate as a transfer of corporate property to one who is a party to an unauthorized act."

Petitioners contend on page 13 of their brief that Section 45 of the Act of 1864 was not a grant of power to national banks, but recognized the existence of the power. The first portion of section 45 is not set out in their brief. The Court, on referring to section 45, heretofore set out in our brief, will note that all national banks designated by the Secretary of the Treasury are expressly made depositories of public funds of the United States and are required to perform such reasonable duties as such depositories of the public moneys as may be required of them; and said section also provides that the Secretary of the Treasury shall require the association to give satisfactory security, etc.

On page 14 of their brief petitioners cite the case of National Bank v. Graham, 100 U. S. 699, in which the power to deliver special deposits was in question. This case is cited as authority for their contention that a power may be granted by a statute by implication. We respect-

fully submit petitioners are very inconsistent in contending that section 45 does not contain a grant of power but is a mere recognition of power, and that section 46 contains a grant of power. The same inconsistency continues in their contention in reference to the various other acts passed by Congress and mentioned in their brief authorizing various government officials to require bond or the pledging of securities for government funds.

POINT V.

A State Bank in Illinois Has No Express Statutory Power to Secure the Deposits of an Illinois Municipality by Pledging the Assets of the Bank.

We find all express powers of Illinois state banks in the General Banking Act, entitled, "An Act to revise the law in relation to banks and banking," approved June 23, 1919, in force December 1, 1920, Chapter 16a, Cahill's 1931 Illinois Revised Statutes. Section 1 of this act is as follows:

> "It shall be lawful to form banks and banking associations, as hereinafter provided, for the purpose of discount and deposit, buying and selling exchange and doing a general banking business, excepting the issuing of bills to circulate as money; and such banks or banking associations shall have the power to loan money on personal and real estate security, and to accept and execute trusts, and shall be subject to all the provisions of this act."

Section 9 of this act prescribed other corporate powers of such banks, and is as follows:

> "Associations organized under this act shall be bodies corporate and politic for the period for which they may be organized, may sue and be sued, may have a common seal which they may alter or renew at pleasure, may own, possess, and may carry as assets the real estate necessary in which to do its banking business, and such other real estate to which it may obtain title in the collection of its debts, but shall not carry in its assets any real estate except its banking house for the period of more than five years after acquiring title to the same.
>
> "No bank shall establish or maintain more than one banking house, or receive deposits, or pay checks at any other place than such banking house, and no banks shall establish or maintain in this or any other state or country any branch bank, nor shall it establish or maintain in this state any branch office or additional office or agency for the purpose of conducting any of its business."

The above sections of the statute prescribed the general corporate powers of a bank in Illinois, and we can find no authority for an Illinois state bank to pledge its assets to secure the deposits of an Illinois municipality in such statute. Therefore, we submit it cannot be successfully contended that an Illinois state bank is given general, express, statutory power to pledge its assets to secure the deposit of an Illinois municipality.

POINT VI.

Neither National Nor State Banks Have Any Implied Power to Secure Deposits of Public Funds by Pledging Their Assets; and it Is Against Public Policy That They Should Have Such Power.

It may generally be said that corporations can only exercise such powers as are conferred in express terms or by necessary implication. The enumeration of powers expressly granted imply the exclusion of all other powers not fairly incidental. An implied or incidental power must be one that exists to enable the corporation to carry out its express powers and it must be in a sense necessary or needful and suitable to accomplish the purpose for which the express powers are granted (People v. Chicago Gas Trust Co., 130 Ill. 268, on page 283; Calumet etc. Dock Co. v. Conkling, 273 Ill. 318, on page 324; National Home Building Assn. v. The Home Savings Bank, 181 Ill. 35, on page 42; Central Transportation Co. v. Pullman Palace Car Co., 139 U. S. 24; People ex rel. v. Seward State Bank, 268 Ill. App. 32 [certiorari applied for and denied by Supreme Court of Illinois]; Farmers and Merchants State Bank v. Consolidated School District, 219 N. W. [Minn.] 163; Smith v. Baltimore and Ohio Railroad Company, 48 Fed. [2d] 861, on page 868, affirmed 56 Fed. [2d] 799).

In the case of Calumet etc. Dock Co. v. Conkling, supra, the Court, after speaking of the authority and power in a corporation to make a loan, on page 322, said:

"Having no express authority to loan money, if it possessed any such authority it must be found in its implied powers. The rule is, that corporations can only exercise such powers as are conferred in express terms or by necessary implication. The implied powers are presumed to exist in order that such bodies may be able to carry out the express powers granted and to accomplish the purpose of the corporation's creation. An implied or incidental power must be directly or immediately appropriate to the execution of the powers expressly granted and not one that has a slight or remote relation to it (People v. Chicago Gas Trust Co., 130 Ill. 268, and cases there cited). The enumeration of power expressly granted implies the exclusion of all others not fairly incidental. A power which the law will imply must be one in a sense necessary or needful and suitable to accomplish the object for which the express powers were granted (Central Transportation Co. v. Pullman Palace Car Co., 139 U. S. 24). Whatever incidental powers are reasonably necessary to enable the corporation to perform its corporate functions are implied from the powers expressly granted (People v. Campbell, 144 N. Y. 166). These general rules are so well settled that further discussion of them or citation of authorities is not required."

We submit that banks, in this respect, are not different from any other corporation, except we think it eminently proper that when a bank claims it has an implied power the rules governing the implied powers of a corporation should be more strictly construed than when applied to private corporations, because banks cannot be considered

altogether as private corporations, but are public corporations created for public purposes.

Banks, among other things, are formed for the purpose of collecting, safeguarding and returning the people's money and at the same time affording a fair return to the stockholders, and anything which tends to destroy any of these purposes should not be countenanced or allowed. We respectfully submit that the wholesale closing of banks in the last few years has to a large extent been caused not from a lack of power, but on account of banks assuming many powers and privileges which they did not have.

Is it necessary for a state bank in Illinois, in order successfully to carry on its business, that it have the implied power secretly to favor a few of its depositors by pledging its assets to secure their deposits? The Supreme Court of Illinois had held in the case of People v. Chicago Gas Trust Company, 130 Ill. 268 (on page 297) that, since the Illinois Constitution of 1870, it has been the public policy of the State of Illinois that special privileges and rights shall not be granted to any corporation, association or individual; that no corporation shall be created by special law, and that the Constitution of 1870 reverses the old policy of granting exclusive privileges to corporations of any kind. It is manifest that the Legislature of Illinois has not seen fit expressly to grant to a bank the right to do those things so strongly condemned in the cases we have heretofore set forth. Can it then be said that an Illinois state bank has the implied power to do those things which,

instead of conducing to the safety of the bank, will in fact result in its insolvency and ruin? We insist that the answer to the above question is "No," and that instead of public policy favoring the securing of deposits by pledge of the assets of the bank, a sound public policy would prohibit such pledges.

The reasoning and law on this point is so well set forth in the case of Farmers and Merchants State Bank v. Consolidated School District, 219 N. W. (Minn.) 163, that we desire to quote from page 165 as follows:

> "The pledge of assets to secure bank deposits falls automatically within that condemnation. At the outset it evinces a willingness to favor the secured depositor at the expense of those less favored. Then it actually sets apart for his exclusive benefit part of a fund to no part of which he should have any such right, and in every part of which the other depositors should have the same right as himself. It is in derogation of that fair and equal treatment of all depositors which is fundamental in the ethics of banking. A conclusive test is that no bank can make a practice of securing deposits by pledging assets and live. A few such transactions made known to its clientele would put any bank out of business. The practice would properly be taken to show that the institution was intrinsically so little deserving of deposits that resort to the too attractive lure of collateral was compelled by adverse circumstances. No bank could long survive such an expose. The very offer of collateral for his deposit would send any discreet and informed de-

positor elsewhere. So, if the practice of securing deposits by pledge of assets is resorted to at all it must be done secretly. That is enough to condemn it. Any power, the exercise of which will not stand the light of publicity, cannot be allowed to banks. The argument that a bank has, as an implied power, one that, if used openly, is ruinous and must be resorted to clandestinely, if at all, refutes itself. Banks are intended, above all else, to be the dependable agents of thrift and commerce. To that end express powers have been conferred on them. It would violate all rules of construction to construe into their implied powers one that would go so far to defeat the purpose of the express powers."

We also quote from the case of Foster v. City of Longview, 26 S. W. (2d) (Tex.) 1059, on page 1061, as follows:

"The financial soundness of the banks of the country is a matter of public concern, and financial soundness vanishes when a bank loses the confidence of its depositors. Sound public policy, therefore, requires that these quasi-public institutions shall so deal with their depositors as to earn and hold their confidence. Nothing, it is thought, could more effectually destroy this confidence and incidentally impair the public usefulness of banks than to allow these institutions, in the absence of specific statutory authority for them to do so, and in the absence of suitable regulations in this regard, to appropriate their assets to the securing of a selected few of their depositors."

In the recent case of State Bank of Commerce v. Stone, decided by the New York Court of Appeals on February

28, 1933, and reported in 261 N. Y. 175, 184 N. E. 750, the Court quoted with approval the above-mentioned quotation from the case of Farmers and Merchants State Bank v. Consolidated School District, supra, and also quotes from the decision in Commercial B. & T. Co. v. Citizens T. & G. Co., 153 Ky. 566, 156 S. W. 160, as follows:

> "This is clearly an act ultra vires and unlawful. No such power has been conferred upon banks in this state, nor should authority to do so be granted anywhere. * * * Large depositors, if secured, might absorb the greater part of the assets of the bank and inflict loss upon unsecured depositors and financial ruin upon innocent stockholders under the double liability law. The law (Banking Law) contemplates, and was evidently framed to insure, fair and uniform dealings by the banks with all of their depositors. A secret pledge to secure one, while others are left without security, although it may be without specific intent to defraud, would nevertheless, in case of loss, justify such an inference. Public policy will not, therefore, tolerate a practice which might, sooner or later, in the event of finding trouble with the bank, enable to pay and protect the favored few at the expense of the equally deserving many. * * * Banks publish statements of their assets and individuals deposit on the faith of these published statements. It is well known that good statements as to assets induce people to deposit their money in banks making such statements. It would be a crowning act of injustice to hold that deposits, thus induced, are nevertheless cut off from sharing in these assets, until some unknown

favored few, who have been secretly secured, are satisfied; and it would be a palpable fraud on the part of a bank thus to procure deposits when its assets were secretly pledged. * * * The aim and trend of all modern legislation on the subject of banks has been to protect the depositor."

Petitioners contend that a state bank in Illinois has power to secure the deposits of a municipality and that such power is implied from the General Banking Act. To sustain this contention they quote Section 11 of the Banking Act, which provides, in substance, that receivers of closed banks shall deposit moneys collected in state or national banks selected by the Auditor, who shall require of such depository satisfactory securities or satisfactory surety bond for the safekeeping and payment of the deposits. It is contended that by this act the Legislature of the State of Illinois has recognized an implied power existing under the General Banking Act. Section 11, above referred to, was submitted to the people of the State of Illinois and adopted by a referendum.

It is submitted that the power of banks in Illinois so to secure deposits of receivers of closed banks is created by section 11 and not by sections 1 and 9. The granting to the Auditor and a receiver of the right to require such securities carries with it the grant to the bank to pledge the securities. In National Bank v. Graham, 100 U. S. 699, cited on page 14 of the brief of the petitioners, the Court stated:

"The forty-sixth section of the Banking Act of 1864, re-enacted in the Revised Statutes of the United States, Sec. 5228, declares that, after the failure of a national bank to pay its circulating notes, etc., 'it shall not be lawful for the association suffering the same to pay out any of its notes, discount any notes or bills, or otherwise prosecute the business of banking except to receive and safely keep moneys belonging to it, and to deliver special deposits.' This implied clearly that a national bank, as a part of its legitimate business, may receive such 'special deposits'; and this implication is as effectual as an express declaration of the same thing would have been (United States v. Babbit, 1 Black 55)."

Likewise section 11 grants a power by implication rather than recognizing an implied power under the general language of sections 1 and 9.

Petitioners also contend that Section 10 of the State Depositary Act, cited on page 35 of their brief, which provides, in substance, that no money in the State Treasury shall be deposited in any bank approved as a depository under the terms of the act until such bank shall have deposited securities with the State Treasurer equal in market value to the amount of the money deposited, also recognizes an implied power under the general language of sections 1 and 9. As heretofore pointed out in our brief, the State of Illinois by virtue of its sovereign powers has a right to priority of payment of all debts due to it from an insolvent state bank. This, in many ways, is the same as the

state having a lien upon all of the assets of such bank. In that well established rule in the State of Illinois there is no element of a grant of power to a bank. The State, by virtue of its sovereign powers, simply demands and takes the State's sovereign right. If that sovereign power exists under the common law of the State, it can be utilized by the State by legislation. By that statute the State of Illinois takes unto itself a lien upon specific assets of banks becoming state depositories.

Since the State, in passing Section 10 of the Depositary Act merely utilized its inherent power to have state deposits secured and did not grant any power to the bank, said section 10 was not an amendment to the Banking Act, and it was not necessary to submit it to a referendum.

POINT VII.

There Is a Manifest Distinction Between the Relation Which an Illinois State Bank Bears to Its General Depositors and That Which the Bank Bears to Persons From Whom It Has Borrowed Money.

There is much difference of opinion among the courts of the various states as to the power of a bank to pledge its assets to secure its deposits. Much of this difference of opinion, we believe, arises from the fact that those courts holding that banks do have the right to secure their deposits by pledging their assets fail to distinguish between the relation that a bank bears to its depositors and the relation which a bank bears to those from whom

it has borrowed money. This distinction is well set forth in the opinion of Judge Sparks rendered in the case at bar (64 Fed. [2d] 721). We quote from Judge Sparks as follows:

> "It is argued that inasmuch as a bank may pledge its bills receivable to secure **loans**, by analogy the power to secure a **deposit** in like manner exists. That argument is based upon the premise that there is no real difference between a deposit and a loan, and that in either case the relation of debtor and creditor arises. It is true that there are certain characteristics which are common to each, but we think the later and better reasoned opinions hold that there is a vast difference. To define that difference with exactness would indeed be difficult, and for the purposes of this case it is quite unnecessary to do so. It is sufficient to say that the difference has always been recognized by the bankers both in theory and in practice, and their method of bookkeeping and their published reports fail to reveal any basis for an analogy. The United States Government and the various states, including Illinois, recognize the difference as shown by the reports which they require to be published. Congress and the various legislatures have recognized the difference over a period of many years by making it a criminal offense for an insolvent bank to receive **deposits**. This has been done obviously for the purpose of protecting depositors; while on the other hand the overwhelming weight of authority is that a bank has the power to borrow money to meet an emergency or an exigency, such as threatened or temporary insolvency. (See Divide County v. Baird, 55 N. D. 45, 212 N. W. 236)."

On this point we also quote from the opinion in the case of Farmers State Bank v. County of Marshall, 221 N. W. (Minn.) 242, where, in answer to the contention that the relation of ordinary debtor and creditor existed, the Court, on page 243, said:

> "In our former decision we tried to show that the duty of a bank to its depositors put it in a situation different from that of the ordinary debtor, and that among its powers was none generally to pledge its assets to secure deposits. * * * It is no answer to say that a bank might go to another bank, borrow the money wherewith to pay the depositor, and give security for money so borrowed. It does not affect the present problem that by such a transaction the other creditors of the bank would be as much prejudiced as by a pledge to the depositor himself. That is because of the basic and far-reaching difference, which we have already dealt with sufficiently, between the ordinary borrowing by a bank and the ordinary deposit therein. The difference is fundamental and in nowise modified by an extension of time on a past-due deposit. * * * The bank, unlike the ordinary debtor, is created by the state and exists under state regulation for the very purpose of receiving and paying deposits without preference between depositors. The conventional debtor is in no such situation, and the argument from analogy fails."

Likewise, in the case of Foster v. City of Longview, 26 S. W. (Texas) 1059, which was a case involving the deposit of public money of the City of Longview, the Court

pointed out the difference between a depositor and a borrower, where, on page 1061, it said:

> "On the question of the pledge of a bank's assets to secure a depositor being contrary to public policy, unless specifically authorized by statute, the courts of other states are not in accord. The basic reasoning upon which the negative view is maintained by courts holding to that view is to the effect that, inasmuch as any bank has the implied power to pledge its assets to secure a creditor, and inasmuch as a depositor is regarded in law as a creditor of the bank, a pledge of the bank's assets to secure a depositor is neither ultra vires nor illegal. Although we readily concede that a depositor is regarded in law as a creditor of the bank, and in some respects is to be treated as being on the same plane with an ordinary creditor, we do not concede that the relation of a depositor to the bank is in all respects the same as that of an ordinary creditor. Depositors constitute the main source from which any bank must receive the funds necessary to carry on its business. * * * The financial soundness of the banks of the country is a matter of public concern, and financial soundness vanishes when a bank loses the confidence of its depositors. * * * Nothing, it is thought, could more effectually destroy this confidence, and, incidentally, impair the public usefulness of banks than to allow these institutions, in the absence of specific statutory authority for them to do so, and in the absence of suitable regulations in this regard, to appropriate their assets to the securing of a selected few of their depositors."

This point is also brought out in the case of State Bank

of Commerce v. Stone, supra, where the Court, in speaking of the contention that the powers to give security for bank deposits and bank borrowings were alike, said:

> "That seems to us unsound. Bank deposits and bank borrowings are alike in but the one respect, that one result of each is the relation of debtor and creditor. In every other respect the two operations are not only different, but in complete antithesis."

It is true that when a bank receives money as a deposit and that when a bank borrows money the relation of debtor and creditor is created, but there the similarity ends. Our Legislature and the courts of Illinois have recognized a marked distinction between an Illinois state bank receiving money on deposit and borrowing money. For illustration, the Legislature has enacted as a portion of the Criminal Code (Ch. 38, Par. 38, Cahill's 1933 Illinois Revised Statutes), in substance, that if any officer of an incorporated bank in Illinois receives a deposit when the bank is insolvent, then such officer shall be guilty of embezzlement, etc. Likewise, it is pointed out in the case of Delano v. Case, 17 Ill. App. 531, affirmed in 121 Ill. Sup. 247, that the directors are in a certain sense trustees for the depositors. It is manifest that no such relation exists between the bank or its directors and a person from whom the bank has borrowed money in the due course of business.

The public policy of Illinois, in reference to the exer-

cise of powers by banking institutions, is well stated in the case of People v. Seward State Bank, 268 Ill. App. 32, from which we quote as follows:

> "The law of this state contemplates fair and uniform dealing by banks with all their depositors, and any secret agreement to protect one while others are left without security, even though no actual fraudulent intent is apparent, is nevertheless absolutely void and of no effect (Commercial Banking & Trust Co. v. Citizens' Trust & Guaranty Co., 153 Ky. 566, 45 L. R. A. [n. s.] 950).
>
> "Banking corporations, being creatures of law, possess only such powers as are expressly granted by law or are impliedly granted because necessary to carry out powers expressly granted, and the making of secret agreements for the benefit or protection of one depositor, as herein attempted, does not fall in either class.".

It will be noted the Court, in support of this doctrine, cited with approval the case of Commercial Banking & Trust Co. v. Citizens' Trust & Guaranty Co., 153 Ky. 566, 156 S. W. 160, which held that the bank had no power to pledge its assets to secure public funds, and is very similar to the case at bar.

In the Seward State Bank case a petition for writ of certiorari was presented to the Supreme Court of Illinois and denied by that Court.

Ward v. Johnson, 95 Ill. 215.

The case of Ward v. Johnson is ably discussed at length by Judge Sparks, and we find it difficult to add anything Judge Sparks has not already said.

We do not believe this case supports petitioners' contention that Illinois state banks have the implied power to secure deposits by pledge of their assets, nor that such implied power was recognized by the Illinois Legislature in passing the General Banking Act. It will be noted the Merchants, Farmers & Mechanics Savings Bank was not organized under general law, but had a special charter granting it many powers not now vested in state banks. It, therefore, cannot be contended that the Legislature, in passing a general banking act, intended to grant to all banks the powers judicially determined to have been vested in Illinois banks organized under a special act of the Legislature. The special charter gave the bank power to

> "* * * make such special regulations in reference to trust funds, deposits or savings as shall best aid the depositors and parties interested, by accumulating and increasing the same, allowing and receiving such rate of interest therefor, not greater than hereinbefore mentioned, as may be agreed upon * * *."

The charter further provided:

> "The business of said corporation shall be con-

ducted by the directors, and in such manner as they may direct."

The Court, in the first sentence of its opinion, said:

"The principal question arising upon this record is, did 'The Merchants, Farmers & Mechanics Savings Bank' have power to borrow money and issue 'investment certificates' therefor, secured by trust deed, as was here done?"

On pages 236 and 237 we quote from the Court's decision:

"Sec. 3. The said corporation shall be authorized to receive money from any person or persons who may wish to deposit the same. * * *

"Thus, it will be seen, express power is given to receive money on deposit * * *.

"In addition to these express powers, there can be no doubt that such corporations possess, also, the implied power to borrow money. * * *"

Evidently the exercise of powers by banks organized under special acts of the Legislature granting to them varied powers did not meet with the approval of the Legislature, and a uniform banking act was deemed advisable to correct the evils of this system.

That the Supreme Court of Illinois has considered the "investment certificates" in controversy in the Ward v. Johnson case as a loan of money to the bank and not as a deposit is further borne out by the case of Alton Mfg.

Co. v. Garrett Biblical Institute, 243 Ill. 298, where the Court, in speaking upon the implied powers of a corporation to borrow money, on page 302 quoted from the case of Ward v. Johnson as follows:

> "This power to borrow is not limited either to particular kinds of corporations or to those organized for any particular purpose, but is possessed practically by all corporations whose business or objects may render it necessary or proper to resort to this method of raising money."

If the "investment certificates" in the Ward case were in fact loans, then the question of the power of an Illinois state bank to secure its general depositors by pledging its assets was not in issue.

The Ward case has been considered and explained at length in the following cases: Smith v. Baltimore & Ohio Railroad Co., 48 Fed. (2d) 861, on page 868; Farmers and Merchants State Bank v. Consolidated School District, 219 N. W. 163, on page 165, and State Bank of Commerce v. Stone, 261 N. Y. 175, 184 N. E. 750.

POINT VIII.

The Illinois Commission Form of Government Act and the Amendment of June 25, 1930, of the National Bank Act, Constituted the Sole Authority and Prescribed the Only Method by Which the City National Bank of Herrin, Illinois, Could Lawfully Secure the Deposit in Question of the City of Marion, Illinois.

The only express authority that a state bank in Illinois has in any respect to secure the deposit of public moneys of a city organized under the Commission Form of Government Act is contained in Section 51 of the Commission Form of Government Act (Cahill's Illinois Revised Statutes 1931, page 412), which provides as follows:

> "In addition to the other duties now imposed by law upon the treasurer of any city or village, the said treasurer shall make his daily deposits of such sums of money as shall be received by him from all sources of revenue whatsoever to his credit as treasurer of said city or village, in one or more banks situated in said city or village, to be selected by the president of said council, the commissioner of accounts and finance, and the treasurer of such city or village, or by any two of them, and any such bank, before any such deposit is made therein, shall be required to enter into an obligation with the said council to pay into the treasury of such city or village interest on the monthly balances of such deposits at a rate to be fixed by the president of said council, the commissioner of accounts and finance, and the treasurer, or by any two of them, and which rate may be changed in the same

manner—such rate to be not less than three (3) per centum per annum, and shall also execute a good (and) sufficient bond, with sureties to be approved by the president of the said council, and conditioned that such bank will safely keep and account for, and pay over said money. Said president of the council, the commissioner of accounts and finance and the treasurer, in the selection of any such depositary bank, shall take into consideration the reputation and solvency thereof, and the sufficiency of the security offered by such bank. All interest paid by any such bank upon such balances shall be collected by the treasurer of said city or village, and shall be by him reported in his next statement following such collection, and shall be considered and treated as a part of the general fund of such city or village, subject to use for any legitimate municipal purpose."

Since the above-mentioned section of the Commission Form of Government Act constitutes the only statutory authority for an Illinois state bank to secure the deposits of a city organized under the Illinois Commission Form of Government Act, and since the 1930 amendment to the National Bank Act provides in substance that a national bank located in Illinois shall have power to secure the deposits of an Illinois municipality organized under the Commission Form of Government Act to the same extent that a state bank has the same authority, it then necessarily follows that said Section 51 of said Act and the 1930 amendment to the National Bank Act constituted the sole express statutory authority for the City National Bank of

Herrin, Illinois, to secure the deposits of the City of Marion, Illinois.

It will be noted that section 51 of the above-mentioned act did not give a bank any power to pledge its assets, but merely provided that before any deposit was made in the bank, it must give bond with surety, etc. Such giving of the bond would not increase the liability of the bank beyond what it incurred at the time the deposit was made, nor would it give the city any additional rights with reference to the assets of the bank not held by a general creditor of the bank. The additional security the city received from the giving of the bond by the bank to the city would arise by reason of the liability of the surety on the bank's bond. The rights of the city against the bank would be to participate in all the assets of the bank as a general creditor, and if the city did not secure payment of its deposit in full, it could then have recourse against the surety. Thus, the relation created between the bank and the city would be the same relation and only the same relation as existed between the bank and all other general depositors.

In the case at bar, since the bank had no statutory authority to pledge its assets to the City, it attempted to do indirectly what it could not do directly, in that it pledged its securities with a third person for the attempted use and benefit of the City, and also of the surety company signing the Treasurer's bond. The case at bar is in many respects similar to the case of Commercial Bank and Trust

Company v. The Citizens Trust and Guaranty Company, 153 Ky. 566, 156 S. W. 160. In the Kentucky case the Treasurer of Jefferson County desired to deposit the public funds in a bank. The guaranty company became surety on a bond given to the Treasurer by the bank, and the bank deposited with the guaranty company $100,000 of its assets. In said case the Court held such deposit illegal and void as being against public policy, and that the bank had no implied power to do such act, and on page 165 the Court announced the rule that where, by a charter provision or statute, a bank is required to secure state, county, court or other deposits before it can receive such deposits, the security which the bank gives must be such as it can procure by personal endorsement or otherwise, which does not involve a pledge of its assets. The reasoning in this case is very applicable to the case at bar. The Illinois Legislature has provided that an Illinois bank, if it wishes to receive deposits of public moneys of a city under the Commission Form of Government Act, must give the city a bond, and we think the language of the Court in the above mentioned case, as found on pages 165 and 166 of the decision, is very applicable:

> "In other words, the Legislature evidently did not intend that the security of any depositor should be impaired in order that that of another might be increased. So the only reasonable construction that can be placed upon these statutes requiring certain public funds to be secured by the depository is that the

security that such depository shall give must be other than a pledge of its own assets.

"There is no statute requiring the deposits of the County Treasurer to be secured by the depository, and there is no express power under which the bank was authorized to secure him by a pledge of its assets; no necessity existed for its doing so, in order to enable it properly to conduct its business as a banking institution; hence, its attempt to do so was an act ultra vires and void."

It will further be noted that Section 51 of the Commission Form of Government Act above mentioned does not in any respect pretend to give the bank power to pledge its assets. Petitioners' contention that the Legislature by the enactment of section 51 impliedly authorized the bank to pledge its assets to the surety executing its bond is reading something into the statute which is not there, and petitioners' position is well answered in the Kentucky case above mentioned, where the Court, on page 164, says:

"Before a bank should be adjudged entitled to exercise any power not expressly given, it should be clearly established that such power is essential to the proper conduct of its business, and necessary to enable it properly to enjoy, use and carry out its express powers. When such test is applied to the claim of right, on the part of a bank, to prefer one of its depositors over another, it is apparent that the right should be denied. The exercise of such a power would necessarily be fraught with great possibilities for the perpetration of fraud, and would undoubtedly have a

tendency to destroy the faith of the depositing public in banking institutions.

"When a legislative act is susceptible of a dual construction, one of which secures equality and equity, and the other paves the way to the perpetration of fraud, no court would hesitate to adopt that construction insuring fair dealing."

Again, on page 41 of their brief, petitioners say that the Legislature was undoubtedly aware of the usual practice of individual as well as corporate sureties to demand and receive indemnity for the obligations they assumed. No evidence of this so-called practice is in the record, and we take issue with petitioners' statement that such is the practice. On the contrary, we submit that such is not the practice, and that practically all surety bonds are issued without the principal of the bond indemnifying the surety in any way.

The case of Divide County v. Baird, 212 N. W. (N. Dak.) 236, is very similar to the case at bar, in that the statute of North Dakota is very similar to the Illinois statute. In the Divide County case the County Board desired to deposit its funds in the bank. The bank furnished a bond and various securities of the bank were deposited. The bank became insolvent and suit was brought for the return of the securities. In the Divide County case the statute of North Dakota, with reference to deposits of public funds in banks, was as follows:

"All funds of public corporations shall be deposited in banks which have been duly designated as depositories of public funds; that no deposit shall be made (except in the Bank of North Dakota) until the depository shall furnish a bond * * * in an amount that shall, at least, equal the largest deposit that may at any time be in such depository."

The Court in this case held that the bank had no power to pledge its assets, and that any such pledge was illegal and void.

POINT IX.

The Receiver Had Power to Disaffirm the Ultra Vires Act of Pledging the Securities and Was Under No Obligation to Return the Deposit.

If the pledge of the assets in question was beyond the power of the bank, it was unlawful and void; and the Receiver is not estopped from disaffirming it and recovering the securities. In speaking of the right to disaffirm an ultra vires contract made by a corporation, the Supreme Court of Illinois, in the case of National Home Building Assn. v. The Home Savings Bank, 181 Ill. 35, on page 44, said:

"The powers delegated by the state to the corporation are matters of public law, of which no one can plead ignorance. A party dealing with a corporation having limited and delegated powers conferred by law is chargeable with notice of them and their limitations,

and cannot plead ignorance in avoidance of the defense."

Quoting from the case of Thomas v. West Jersey Railroad Company, 101 U. S. 71, the Supreme Court of Illinois, in the above-mentioned case, in reference to invoking the doctrine of estoppel, on page 45, said:

> "To hold that this can be done is, in our opinion, to hold that any act done under a void contract makes all its parts valid, and that the more you do under a contract forbidden by law the stronger the claim to its enforcement in the courts."

In the case of Wood v. Imperial Irrigation District, 216 Calif. 748, 17 Pac. (2d) 128, the Supreme Court of California, in holding that the receiver of a bank had power to disaffirm the unlawful pledge of securities without returning the deposit, said:

> "Appellant complains somewhat bitterly, and probably not without color of moral justification, and invokes the doctrine of estoppel against said bank, based upon the stipulated fact that said bank solicited said deposits, and had it known that the bank could not have lawfully pledged its bonds it would not have made the deposits. It is also stipulated that the Superintendent of Banks was charged with knowledge that the pledged bonds were in possession of the district for more than two years, and he made no complaint as to its possession and claim. The difficulty with this proposition is that the rights of the deposi-

tors, innocent third parties, are involved in the transaction, and their protection is one of the first concerns of the law. Their rights are surely equal with those of the district, unless the statute has given a preference to said district, which was an actor in the transaction. If it acted under a mistake of law, its position should not be better than that of other depositors who were ignorant of the bank's approaching insolvency, as well as the attempt on the part of the district to secretly secure its deposits."

We think Judge Sparks, in the majority opinion in this case, concisely set forth the law, and we quote from him as follows:

"It does not appear to us as worthy of judicial approval that the secured depositor may take advantage of the ultra vires act of the bank and assert an estoppel grounded upon such act. It had no right in making the deposit to rely upon a preference in the form of an unlawful transfer of assets. Otherwise, both parties, bound to realize the illegality of the transfer, might, in the face of such unlawfulness, agree to make the transfer, saying each to the other, 'though the transfer is not authorized by law, yet we will make it and accomplish the desired result, despite its illegality, for neither may hereafter rescind without restoring the original status.' We do not approve of the accomplishment of an illegal result by way of any such unconscionable use of the doctrine of estoppel. We hold with the decisions in the case cited that the Receiver may repudiate the invalid pledge without returning the valid deposit, and that appellees must

share with the other general depositors in the distribution of the bank's assets."

The following cases likewise support our contention that the Receiver was authorized to disaffirm the ultra vires pledge: Baltimore and Ohio Railroad Co. v. Smith, 56 Fed. (2d) 799; Austin v. Lamar, 26 S. W. (2d) 1062; Calumet etc. Dock Co. v. Conkling, 273 Ill. 318; Farmers and Merchants State Bank v. Consolidated School District, 219 N. W. 163.

It is suggested in the case of State Bank of Commerce v. Stone, 261 N. Y. 175, 184 N. E. 750, that the remedy lies in examinations by the administrative officers in charge of banks. In the very nature of things pledges of assets for deposits are more likely to be demanded at a time when the banks are in failing circumstances and they are more likely to accede to such demands at such times because of their need of funds. Examinations can be made only at intervals and if the bank is in failing circumstances it is a matter of common knowledge that deposits may be secured by pledges and the banks closed before an examination is made. Further, the very demand by examining officials that a failing bank return all deposits secured and regain the pledged assets, might, because of the bank's depleted cash position, force the bank to close, leaving the assets still pledged. In the case at bar the deposits were made and the collateral pledged between the 25th of August, 1931, and the 21st of October, 1931, on which last-

mentioned day the bank closed. Thus, less than sixty days intervened between the delivery of the collateral and the closing of the bank. Cases are rising in courts throughout the nation on violations of banking laws, both civil and criminal, by officers of banks, and such violations were not prevented by examinations.

In petitioners' brief, it is contended that if petitioners are permitted to retain the benefits of the collateral pledged, the general creditors of the City National Bank of Herrin have suffered no injury. It is stated that such creditors have been benefited to the extent of the deposits made in that there remains in the assets of the bank cash in the amount of such deposits, which cash would not be there for their benefit if the deposits had not been made and the collateral pledged. Such theory, viewed in the light of facts surrounding the closing of banks in the trying period through which we have been passing, is untenable. During the past few years knowledge of the manner of closing of banks has been impressed upon everyone having any dealings with such institutions. Depositors, losing confidence, start making withdrawals. As the amounts of such withdrawals become alarming, banks eagerly seek cash by sale of assets, borrowing and solicitation of deposits. The demands of withdrawing depositors usually are met as long as there is cash available, and, in most cases, the banks remain open as long as there appears to be sufficient cash with which to settle immediate demands. Deposits made during such "runs" are not used by the

banks in granting loans or in purchasing securities, but are used to discharge the obligations of withdrawing depositors. When the cash of the bank is thus depleted the bank closes. Consequently, the deposits made during such period do not remain among the assets of the bank, but have been dissipated in paying the obligations to other depositors and, in so far as the remaining depositors are concerned, the only benefit derived by them from such deposits is that the obligation of the bank to some other depositor, or depositors, has been discharged. In terms of money benefit to the remaining creditors of the bank, this means that the assets of the bank in the hands of the receiver are not chargeable with dividend payments to the withdrawing depositors whose claims have been satisfied by the cash placed in the bank by the late depositors. If one of those late depositors is secured by pledge of assets, as in the case at bar, and is permitted to retain those assets, the result is that such collateral is lost to the general creditors and their benefit is measured by the dividends which would have been paid to the withdrawing depositor whose claim was paid by the deposit of the secured creditor. It is exactly this benefit which the respondent offers to restore to the petitioners.

Petitioners take the position that the burden is upon respondent to show that the City National Bank of Herrin **did not** have the power to pledge the securities in question. We insist the burden is upon petitioners to show that the bank **did have** the power, as is stated by Justice Baldwin

in his dissenting opinion in the case of United States v. Robertson, 5 Pet. (U. S.) 641, where he says:

> "The injured creditors are not bound to show a negative of the power by any restrictions or prohibitions. It is an universal principle, that he who claims under a special authority must show its existence and lawful exercise: to throw the burthen of proof on the party whose rights will be destroyed by its abuse, would be the utter reversal of every rule which governs * * *."

CITY OF CHICAGO AS AMICUS CURIAE.

We have read with a great deal of interest the matters called to the attention of this Court by the City of Chicago, as amicus curiae. While the condition of the City of Chicago may be of great general interest, we respectfully submit that such matters are not contained in the record and are not properly before this Court in the determination of the issues involved in this case.

Respondent respectfully submits that the decree of the Circuit Court of Appeals should be affirmed.

HOSEA V. FERRELL,
JOHN HAY,
Counsel for Respondent.